ESOP TERMINOLOGY

ESOP	Stands for Employee Stock Ownership Plan, which is an employee benefit plan known as a defined contribution plan that must be primarily invested in employer securities and which may use borrowed money to acquire the employer securities.
Employer Securities	This term, for ESOP purposes, is defined as common stock issued by an employer that is readily tradable on an established securities market. If there is no class of common stock that is readily tradable, employer securities generally means common stock issued by an employer having a combination of voting power and dividend rights equal to or greater than the class of common stock having the greatest voting power and the class of common stock having the greatest dividend rights. In most ESOP companies the employer securities are referred to as company stock.
Privately-held	Refers to a corporation where stock is not traded on a recognized stock market.
Publicly-traded	Refers to a corporation where stock may be purchased through a market, which facilitates matching those persons wanting to purchase stock with persons wanting to sell the stock.
C Corporation	A company that is treated just like a person under federal income tax laws, in that the company pays a federal income tax on its taxable income. In general, shareholders pay tax again on profits, or dividends received from the C corporation. Thus two levels of federal income tax may be paid on C corporations' taxable income.
S Corporation	A corporation that does not pay federal tax on its income, but instead shareholders of the corporation report their pro rata share of the S corporation's taxable income on their own personal tax returns.
Dividends	In general, the term applied to a C corporation's payment of money from its corporate level income to shareholders. With regard to ESOPs, dividends paid based on ESOP shares are, in certain circumstances, deductible by the corporation from its income for federal tax purposes. The corporate level deduction for dividends paid on ESOP shares means that the double taxation on the income paid as dividends is eliminated.
Leveraged	With reference to an ESOP, means that borrowed money purchased the employer securities of the employer to be assets of the ESOPs. The employer securities purchased with the borrowed money may initially be pledged as security for the loan and are held by the ESOP trust in a "suspense account," and released to employee accounts on a pro rata basis, as the loan is repaid.
Non Leveraged	An ESOP that receives contributions of stock from the corporate sponsor or purchases stock using money contributed by the corporate sponsor, but the money was not borrowed.

Administration	A term referring to the process of maintaining records and reviewing transactions associated with an ESOP. These duties can be the responsibility of one person or multiple people and or companies.
Diversification	In general, refers to having many different kinds of assets in a retirement savings plan. With regard to ESOPs, most often refers to the legal requirement that participants in an ESOP who have participated in the ESOP for ten years and who are 55 or older may convert up to 50% of their stock in their ESOP account over six years to cash, or assets that are not company stock.
Distribution	With reference to an ERISA plan distribution, such as an ESOP, the term means transferring assets, such as stock or cash, to an ERISA plan participant who has retired, died, become disabled, or left the employment of the ESOP sponsor. Sometimes there are "early" distributions to an active employee participant from an ERISA plan, which creates unique individual tax issues. "Distribution," when used in reference to an S corporation, can have a very different meaning. When an S corporation pays money to its shareholders from its profits, it is also referred to as a distribution. To avoid confusion, many ESOP experts refer to an "ERISA distribution" or to an "S corp distribution from current earnings."
Put Option	With reference to ESOPs means that a participant receiving a distribution of stock from an ESOP sponsored by a privately-held company can sell the stock back to the ESOP sponsor, or in some circumstances, the ESOP.
Repurchase Obligation	With reference to ESOPs means the obligation of a privately-held company to buy back its stock distributed from the ESOP to retired, deceased, disabled or terminated employees.
Summary Plan Document	Also referred to as the ESOP Plan Document, this is a summary of the legally required binding document for a company's ERISA plan, which would include an ESOP.
ERISA	Stands for Employee Retirement Income Security Act. Passed into law in 1974, ERISA is the federal law that governs all tax qualified deferred compensation plans, including ESOPs.
Valuation	This refers to the legal requirement that every year an independent expert or firm review the privately-held company sponsor of an ESOP to determine its value as measured in dollars. The total value is divided by the number of shares the corporation has, and each share is thus assigned a value. In a publicly-held corporation with an ESOP, the value of shares are in essence the price paid for shares in recent buy-sell transactions in the market. Sometimes, a valuation of a privately-held ESOP sponsor is done in connection with a major transaction by the company, such as a merger or sale of the company.

Vesting — A term referring to the time when a participant is entitled to the plan's assets in his or her account if he or she retires, dies, becomes disabled, or leaves the company sponsoring the ERISA plan, such as an ESOP. Federal law prescribes minimum vesting schedules, and an ESOP sponsor can choose which to follow, or have vesting different from the law if the vesting is more rapid than the schedule prescribed by law.

Voting Rights — This references the legal requirement that owners of stock vote on certain actions of the corporate issuer of the stock. In an ESOP, the trust is the legal owner of the stock, thus the trustee votes the stock on those actions requiring a vote under corporate laws where the ESOP company is incorporated. In a publicly-traded company, the ESOP trustee generally follows directions from ESOP participants on how to vote stock that is in the employees' accounts. In a privately-held company, the trustee votes the stock as directed by employees on certain issues only.

Fiduciary — A term referring to someone who acts in a position of trust on behalf of, or for the benefit of, a third party. ERISA requires plan fiduciaries (who include anyone exercising discretionary authority or control over the ESOP or any authority or control over ESOP assets) not only to act in the exclusive interest of plan participants but also to act prudently.

IRC — Refers to the Internal Revenue Code

Dr. Louis O. Kelso — He developed the ESOP concept, among others, based on his theories of finance and expanding capital ownership in a more equitable manner. He reasoned that only through widespread capital ownership could capitalism be sustained. He died in 1991.

Senator Russell B. Long — The Chairman and ranking member of the Senate Committee on Finance in the United States Senate for over twenty years, representing the state of Louisiana. He is regarded as the "legislative" father of ESOPs, and from 1972 until his retirement in 1987 he worked diligently and "championed" the ESOP cause on Capitol Hill. He died in 2003.

The ESOP Association — A national non-profit association of employee-owned companies and ESOP practitioners. Visit them on the web at www.esopassociation.org.

October — For the past 20 years when we celebrate Employee Ownership Month, it is the celebration of the incredible spirit of employee ownership. It is an opportunity to educate employee owners about the tremendous benefits of employee stock ownership plans. Lastly, it is an opportunity to educate elected officials and the public as to why employee ownership through ESOPs is good public policy.

Fust Charles Chambers LLP
CERTIFIED PUBLIC ACCOUNTANTS
315.446.3600
5784 Widewaters Parkway
Syracuse, New York 13214
www.FCC-CPA.com